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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)))	MM Docket No. 92-266

COMMENTS OF
THE NATIONAL CABLE TELEVISION ASSOCIATION
ON THE FIFTH NOTICE OF PROPOSED RULEMAKING

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SUMMARY

The Fifth Notice of Proposed Rulemaking seeks comment in two areas: (1) whether the Commission's "going forward" rules should be modified, and (2) whether the Commission should regulate rates cable operators charge to commercial establishments, such as bars, restaurants, and office buildings.

With respect to the Commission's going forward methodology, the Notice provides a needed opportunity for a fresh examination of the going forward rules. The current formula provides virtually no incentives to add programming to regulated tiers. The Commission should act quickly to craft rules that provide such incentives while protecting subscribers against unreasonable rates. Specifically, the formula should be revised to provide operators with a flat fee per channel plus programming costs.

In tandem with changes to its going forward formula, the Commission also must establish more certainty as to how channels can be added on an a la carte basis. There should be clearly defined safe harbors to guide operators' decision-making when creating packages of services. A joint policy on allowable going forward arrangements on regulated tiers and on an a la carte basis will bring needed certainty to a cable programming landscape now devoid of any meaningful activity anywhere.

Finally, the Commission should not regulate rates for cable service to commercial establishments. There is no indication that Congress intended that the Commission dictate rates for non-residential customers. But even if the Commission does have authority to act in this area, it should not require operators to charge commercial subscribers the same rates as residential customers.

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The National Cable Television Association, Inc. ("NCTA"), by its attorneys, hereby submits its comments in the Fifth Notice of Proposed Rulemaking in the above-captioned proceeding.[1] NCTA is the principal trade association of the cable television industry in the United States. Its members include cable television operators and cable programmers, as well as equipment suppliers and others interested in or affiliated with the cable television industry.

INTRODUCTION

This Fifth NPRM provides a needed opportunity for a fresh look at the important issue of how rates for cable systems should be adjusted when channels are added to regulated tiers. It asks whether "the Commission's going forward methodology should be modified to provide greater or lesser compensation to operators for adjustments to capped rates when channels are added or deleted from regulated tiers, and whether this would better meet our goals of

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1 Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266 (rel. Mar. 30, 1994) at ¶¶ 254-257 (hereinafter "Fifth NPRM").

encouraging infrastructure development and growth of programming".[2] Modification to the going forward methodology is essential to provide an environment in which diverse programming services can continue to grow. Otherwise, the Commission will have accomplished its goal of reducing rates only at the expense of a vibrant programming industry.

While Congress may have intended to curb unreasonable rates in adopting the Cable Act, it did not intend that the balance would be tilted so heavily toward low rates that programming diversity would be stifled. Rather, the Act was also designed to "promote the availability to the public of a diversity of views and information through cable television and other video distribution media," and to "rely on the marketplace, to the maximum extent feasible, to achieve that availability." Congress also desired to "ensure that cable operators continue to expand, where economically justified, their capacity and the programs offered over their cable system."[3]

The Commission acknowledged that the goal of its "going forward" rules should be to "allow cable operators to grow and develop new facilities and services, including new and innovative regulated programming services."[4] Nonetheless, by adopting a percentage markup and providing for only a minimal benchmark "adjustment factor" when channels are added, the methodology unfortunately does not accomplish this goal. In fact, the methodology has precisely the opposite effect, and has perpetuated the difficulties faced by programmers in gaining access to cable systems since April 1993.

When the Report and Order was then adopted, the Commission established the general framework for adjustments to permissible rates "going forward". At that time, it stated that

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2 Fifth NPRM at ¶ 256. The NPRM also solicits comments on "whether we should establish regulations governing rates for regulated cable service provided to commercial establishments." Id. at ¶ 257

3 Cable Act, Section 2(b)(1)-(3).

4 Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Fourth Report and Order, MM Docket No. 92-266 (rel. Mar. 30, 1994) at ¶ 238 (hereinafter "Fourth Report and Order").

"forms prescribing the precise methodology for calculating [future rate adjustments] . . . on a going-forward basis will be released shortly."[5] Last summer, the Commission issued a Third Further Notice of Proposed Rulemaking specifically soliciting comments on rate adjustments where channels are added to, or deleted from, regulated tiers.[6]

From April 1993 until the release of the "going forward" rules nearly a year later, relatively few cable program networks were added to regulated tiers.[7] Operators and programmers did not know the rules under which adjustments to rates would be allowed, and the FCC-imposed rate freeze prevented operators from adding programming services to existing tiers and recovering their costs.[8] Now that the rules are known, and the rate freeze lifted, a thaw has failed to materialize. The numerous cable operator and programmer comments already filed in this Docket attest that the incentives contained in the FCC's rules for cable operators to add channels to regulated tiers are virtually non-existent.[9]

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5 Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Report and Order, 8 FCC Rcd. 5631, 5789 n.604 (1993) (hereinafter "Report and Order").

6 Third Notice of Proposed Rulemaking, MM Docket No. 92-266 (rel. Aug. 27, 1993).

7 See Kagan, Cable TV Programming (Dec. 29, 1993) (describing how lack of channel capacity and regulatory environment made "prospects for new networks through the first half of 1994. . . grim.").

8 Some existing networks did gain carriage as of September 1993, however, as a result of operators adding more program networks as part of an effort to bring their tier rates into compliance with the benchmarks contained in the April 1993 Report and Order.

9 See, e.g., Response of Continental Cablevision, Inc. in MM Docket No 92-266 (filed June 16, 1994); Comments of the Times Mirror Company (filed May 16, 1994); Viacom Petition for Reconsideration (filed May 16, 1994); Comments of Programming Providers (filed May 16, 1994); Petition of United Video for Reconsideration (filed May 16, 1994); Opposition of Discovery Communications, Inc. (filed June 16, 1994); Comments of Liberty Media Corporation on Petitions for Reconsideration (filed June 16, 1994); Comments for A&E and ESPN in Support of Petitions for Reconsideration (filed June 16, 1994); Comments of Fox Basic Cable, Inc. (filed June 16, 1994); Ex Parte Comments of Cox Cable Communications, Inc. and Newhouse Broadcasting Company (filed May 31, 1994).

The problem is compounded by the lack of certainty as to how channels can be added on an a la carte basis. This regulatory climate has caused significant difficulties for the programming industry. Launches previously planned have been delayed.[10] And services recently launched, such as Americana and the Sci-Fi Channel, have failed to gain expanded carriage.[11]

The Commission has shown sensitivity to these concerns regarding the impact of its rules. And it has demonstrated an open mind to proposed modifications to those rules to provide more incentives for operators, and more opportunities for programmers. The Commission can and should craft rules that do not unduly skew the marketplace for programming, while protecting consumers against unreasonable rates. The Commission should quickly act to establish guidelines -- both for adding channels to regulated tiers and a la carte packages -- so that the cable industry can move ahead and programming investments can continue.

The Commission should consider questions regarding adding channels on a regulated and a la carte basis in tandem. Both approaches are permissible under the statutory scheme, and it is important to allow these marketing systems to develop without undue bias arising from government rules. Resolving only one aspect of program additions will not provide the cable industry with the full picture which is necessary to conduct its future business. Resolving neither side of the calculus will only lead to further paralysis.

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[10] See Kagan, Cable TV Programming (June 23, 1994) at 1 ("The cable programming business is beginning to sound like Cape Canaveral on a really bad day. Reports of launch delays have become a torrent as cable operators . . . have put off plans to add all but a handful of new networks until 1995 -- and then only if key parts of the new rules are modified or tossed out.").

[11] See generally Kagan, Cable TV Programming (May 23, 1994) at 4 (reporting that as a result of regulation, there "[h]as been an almost total stifling of new network launches and additions of incumbent networks to channel lineups."); Kagan, Cable TV Programming (June 23, 1994) at 4 (describing experience of Turner Classic Movies, which launched April 14, 1994; "The majority of TCM subs are TVRO satellite homes . . ., attesting to the current difficult environment for start-up nets seeking shelf space on cable systems.").

I. THE COMMISSION'S "GOING FORWARD" METHODOLOGY MUST BE MODIFIED TO PROVIDE INCENTIVES TO ADD CHANNELS TO REGULATED TIERS OF SERVICE

A. The Commission Should Provide Incentives to Add Channels to Regulated Tiers

Rates under the current going forward methodology are adjusted based on three elements: (1) the cost of the programming to be added; (2) a 7.5% mark up on that programming cost; and (3) a "per channel adjustment factor."[12] The adjustment factor starts at 52 cents for systems with 7 or fewer regulated channels and drops precipitously after that. Systems with more than 17 regulated channels obtain less than a dime; systems with more than 24 or more regulated channels obtain only 5 cents; and systems with more than 46 channels receive only a penny. Virtually all cable subscribers are customers of cable systems with 20 or more regulated channels.[13] The pennies allowed in the channel adjustment factor -- coupled with the minimal mark up on programming costs -- provide systems no incentive for adding channels to regulated tiers.

Under this formula, it will take up to 29 months for an operator with a 47 regulated channel system just to recover the cost of postage for the notice it must send each subscriber when it adds a no-cost program service. This does not even take into account other costs that may be incurred when programming is added, such as purchase and installation of a satellite dish, additional feeds, receivers, modulators, descramblers, and revisions to the program guide and additional marketing expenses.

But there are several reasons -- going beyond the actual costs that may not be recovered -- that explains why the current methodology fails to provide incentives to add channels to

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[12] 47 C.F.R. § 76.922(e).

[13] Based on the FCC's 1992 random sample of cable operators, 99.1 percent of subscribers are served by systems with 20 or more regulated channels.

regulated tiers. First, the "per channel adjustment factor" is calculated in a formulaic manner that fails to account for actual behavior and opportunity costs. Second, the 7.5 percent markup hardly compensates operators for the risks taken and reward expected when using valuable channel space for providing regulated services. And it discriminates against no- and low-cost services -- precisely the types of advertiser-supported services designed to be carried on tiers reaching the greatest number of subscribers. Taken together, it may well be the case that operators would lose money under this formula, if they choose to provide their subscribers with additional program channels.

1. The Per Channel Adjustment Factor Should Be Eliminated

The difficulties with the going forward methodology are inherent in using the declining benchmark formula for deriving the appropriate rate when channels are added. The formula is based on observations of average rates for "competitive systems" in September 1992. It is derived from a look at static rates. While on average the per channel rate may decline as the number of channels increase, rates may well have increased in excess of the average per channel rate for the existing tier when channels were added. The snapshot of rates taken in September 1992 does not indicate how cable systems behaved when channels were added to existing tiers of service on their systems, or what rates would be needed to induce operators to do so in the future.

A significantly more relevant measure of what the appropriate rate should be to provide an incentive to add channels to regulated tiers, therefore, would be based on examining the historical behavior of cable systems when channels were actually added in the past. To ensure that these rates are "reasonable" under existing rules, these observations could be limited to cable systems operating in "effectively competitive" environments. These are the same conditions upon which the Commission has relied in devising the 17% competitive differential, and they presumably would lead to pricing new channels in a manner that reflected competitive marketplace conditions. If these system's historical experiences are examined, the Commission can at least measure rate changes in a dynamic setting, rather than rely on the average rates charged by competitive systems in a static environment.

Another factor not accounted for under the Commission's current rules is that operators are free to use unused channel capacity for either regulated or unregulated services. By failing to provide any breathing room when channels are added on a regulated basis, the Commission's rules strongly favor use of those channels for unregulated purposes, such as pay-per-view or a la carte offerings. In order to ensure that the rules do not tilt against the addition of regulated services, the going forward rules cannot continue to ignore considerations of "opportunity costs" entailed in operators choosing how to make use of an unoccupied channel.

The going forward rules, therefore, should provide latitude so that operators have adequate incentives to continue to provide, and to increase the number of, regulated services. An operator will add a channel to a regulated tier only if the return from doing so covers all relevant costs, including the opportunity cost. Therefore, the profits operators receive from adding a program service to a regulated tier should be at least as great as the incremental profits from alternative uses of the unused channel capacity.

2. The Commission Should Eliminate the Markup on Newly-added Programming

The Commission's rules also should be designed not to skew operators' decisions regarding the type of programming to be added to regulated tiers. Unfortunately, the 7.5 percent markup on programming costs currently contained in the rules has precisely that effect. It discourages an operator from adding low-cost or no-cost program networks on which it will earn virtually no return. And the rule provides artificial incentives for programmers to boost rates to operators so as to induce operators to carry them -- a result that surely does not serve consumers' interests.

New and start-up networks are inherently disadvantaged by this approach. In the absence of these going forward rules, new networks historically have started out with no or minimal license fees to operators in order to induce them to carry them. Basic programmers revenues, therefore, were derived in significant respects from advertising fees that they could obtain from wide distribution to cable viewers.

Under the new rules, the strategy of charging initial low license fees in order to gain viewers will fail to induce operators to carry these programmers. Instead, the only financial reward an operator would receive from carriage of a program network is based on the license fee markup. The marketplace has made clear that this provides no incentive to add channels at all. While 7.5 percent is not an appropriate markup in any event, even a 100 percent markup on a no cost service would fail to alleviate these disincentives to carriage.

3. The Commission Should Adopt a Flat Fee Plus Programming Cost Methodology

For these reasons, the Commission should discard the current reliance on percentage mark-up and the per-channel adjustment factor contained in the going forward methodology. Instead, the Commission should establish rules that enable operators to increase their tier rate by a flat fee per channel plus the programming cost when a channel is added to a regulated tier.

Allowing operators to increase their rates by a flat fee per channel would eliminate the current disincentives to add low- or no-cost channels. And allowing the programming cost to be recovered on top of the flat fee would ensure that more expensive services were not disadvantaged.

Some concern has been expressed that allowing a flat fee, as opposed to percentage markup, enables operators to "game" the system by putting on no-cost services and increasing rates as a way to recover whatever monopoly profits have been lost as a result of rate regulation. But this incorrectly assumes that the fee charged to an operator reflects the value of that service to the public.

Even assuming, arguendo, that evaluation of "quality" by the Commission were constitutionally permissible, there is no reason to equate cost to the operator with quality considerations. As described above, given the economics of basic programming, charging operators low license fees is a business strategy pursued by many programmers, looking to advertising revenues to account for as much as 60% of revenues over the long term and close to 90-100% in the short term. A large number of such attractive program services currently are vying for scarce channel space.[14] Given these numerous choices of valuable programming services currently waiting for carriage, it is highly unlikely that an operator would add the proverbial "fireplace" channel in order to game the rate regulation system. Such a strategy would risk alienating subscribers and triggering oversight from regulators under the evasion standard.

But in seeking to close every potential loophole to protect against the potentially evasive cable operator, the Commission should not lose sight of the goal of incentives. To be sure, the rules now protect against operators adding valueless services merely to increase their rates -- but only because they virtually ensure that no new services will be added to regulated tiers at all. Consumers are surely the losers in this unequal balancing. They are not well-served by rules that would allow new services to expire in order to protect against the remote possibility that an operator would manipulate the system in order to somehow reap a windfall, which in any case would be transparent to viewers and regulators alike.

B. Procedural Obstacles Should Be Modified to Remove Impediments to Adding Channels

The lack of financial incentives to add channels to regulated tiers is not the only barrier created by the Commission's rules. The rules also contain significant procedural obstacles. If the Commission intends to alleviate the difficulties caused by its rules, these procedural roadblocks must be reexamined as well.

For example, under the Commission's current interpretation of its rules, an operator raising a rate where a channel is added to a cable programming service tier opens up that entire

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[14] Dozens of networks intending to rely on either no fee or a combination of license fees and advertiser support are planning to launch. NCTA, Cable Television Developments (Apr. 1994) at 56-C to 66-C.

tier rate to attack by a complaining subscriber.[15] Therefore, an operator that takes a completely lawful rate increase when a channel is added faces the prospect of defending its entire tier rate upon complaint.

This procedure is unwarranted and contrary to the statutory scheme. Congress intended that subscribers could file complaints against rates in place on the effective date of the FCC's rules only for a 180 day period.[16] February 28, 1994 has passed, and many cable systems have not had complaints filed against their cable programming service tier. The rule prolonging the review period of the entire rate is directly counter to the statutory cutoff. And it adds further roadblocks to programmers being added to regulated tiers for those systems whose tier rates have not been challenged to date.

In addition, the Commission should ease the way for operators to add services to regulated tiers by clarifying that additions to such a tier will not trigger an obligation to affirmatively market that tier to existing subscribers. Confusion in this area has arisen based on the Commission's discussion of "concurrent jurisdiction" that may be exercised by state and local governments to regulate "negative options."[17] The Commission previously has made clear that a cable operator that increased its rates when it added channels to regulated tiers or switched out channels would not be engaged in a practice necessitating affirmative marketing of the tier.[18]

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15 See News Release, Feb. 25, 1994 ("In assessing the reasonableness of a rate, the Commission will consider the total rate and not just the most recent rate increase").

16 47 U.S.C. §543(c)(3).

17 See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Third Order on Reconsideration, MM Docket No. 92-266 (rel. Mar. 30, 1994) at ¶ 131.

18 See Report and Order, 8 FCC Rcd. at 5906 ("[a] change in the mix of channels in a tier, including additions or deletions of channels, will not be subject to the negative option billing provision, unless they change the fundamental nature of the tier.")

Indeed, the Commission has recognized that an affirmative marketing requirement in these circumstances could be perceived as a burden, and not a benefit, by subscribers.[19]

Confusion remains in this area, though. While not a negative option under federal law, the Commission should reiterate that state and local governments are preempted from enacting or enforcing laws that may be construed to hold these practices to be prohibited negative options.[20] Otherwise, the possibility that operators at some later date may be found to have violated a state negative option prohibition will act as an additional deterrent to adding channels to regulated tiers.

II. THE COMMISSION MUST ESTABLISH CLEAR GUIDELINES FOR A LA CARTE PACKAGES

While this Fifth NPRM focuses on modifying the "going-forward" methodology, this is only one part of the two means by which program networks will be added to cable systems. Operators also must choose, to the extent contractually permissible, whether to offer networks on an a la carte basis and in packages of a la carte offerings.

The Commission has indicated, however, that packages of a la carte offerings may be considered to be a "regulated" tier in certain circumstances.[21] These circumstances must be clarified so that the ground rules are known by operators and programmers.

The Commission previously set forth a two part test for judging whether a la carte packages were to be considered unregulated: if (1) the price of the combined package did not

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[19] Id.

[20] See Attachment A, Letter to William E. Kennard from Daniel L. Brenner, dated April 26, 1994 (seeking Commission clarification that affirmative marketing does not apply to changes to regulated tiers and that states may not require affirmative marketing in such instances.)

[21] We do not believe that Congress granted the Commission authority to regulate a la carte offerings, and reserve the right to challenge the Commission's authority to do so. See NCTA v. FCC, No. 94-1366 (D.C. Cir., filed May 12, 1994).

exceed the sum of the individual charges for each component of service, and (2) the operators continued to provide the component parts of the package to subscribers individually.[22] This latter test focused on whether a subscriber had a "realistic service choice" to take channels individually, as opposed to the entire package.[23]

The Commission in its most recent Order suggests that it is continuing to adhere to that test, but it now has fifteen additional factors to guide its determination.[24] While intended to provide more clarity, this collection of factors has led to more confusion, not less.

The current uncertainty as to when channels can be added on a a la carte basis has prevented operators from making business decisions regarding the addition of new program services to their system on either a regulated or unregulated basis. The inability to move forward is compounded by the difficulties faced by operators that already have created a la carte packages based on earlier Commission pronouncements. Clearly, many of those packages are entirely consistent with the Commission's rules. But those operators still do not know whether those packages will be considered regulated or unregulated. And finally, the new freedom given to local franchising authorities to make a la carte determinations -- even before the Commission has itself decided what is appropriate or fair[25] -- has exacerbated these difficulties.

It is therefore imperative that the Commission set forth some clear guide posts for operators. The Commission has indicated that guidance will be forthcoming in its resolution of

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[22] Report and Order, 8 FCC Rcd. at 5836-37.

[23] Id. at 5837.

[24] Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Second Order on Reconsideration, MM Docket No. 92-266 (rel. Mar. 30, 1994) (hereinafter "Second Order on Reconsideration.") at ¶ 196.

[25] See generally TKR Cable Company, DA 94-691 (rel. June 23, 1994) (refusing to stay New Jersey Board of Regulatory Commissioners ruling on TKR Cable Company's a la carte offerings).

a number of outstanding Letters of Inquiry , and that "the goal here is to lay out quickly as many understandable and useful models for lawful a la carte offerings as the industry says it needs."[26] That goal can best be accomplished by establishing clearly defined safe harbors.

For example, two of the factors currently set forth by the Commission focus on whether the number or percentage of channels previously carried on a regulated tier and migrated to an a la carte package are "significant" or "insignificant".[27] The Commission recognizes that "[i]ncluding some previously regulated channels may be necessary for the successful marketing of the new package."[28] But while some migration is permissible, no guidance has been given as to how a determination will be made on whether migration of a particular number of regulated services is significant or not. Operators may need flexibility (subject to the contractual relationship between the operator and programmer) to migrate at least some services carried on the system to create attractive a la carte offerings. A balancing of interests should be incorporated in the rules so that a specific policy on the number of channels that may be migrated is established as a safe harbor.[29]

Another of the Commission's factors looks to whether the discount provided to subscribers when they purchase the package instead of individual channels is too "deep". But the Commission previously agreed that discounts are pro-consumer. It made clear that "[c]able operators should be free to offer collective offerings at a combined price which is less than the sum of the charges for the individual services. Such discounts benefit the customer by making

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[26] See Chairman Reed E. Hundt Speech Before the 43rd Annual Convention & Exposition of the National Cable Television Association (May 24, 1994) at 8.

[27] Second Order on Reconsideration at ¶ 196.

[28] Id. at ¶ 196 n. 267.

[29] To the extent the Commission establishes a cap, operators that migrated more than the cap prior to June 1, 1994, should be given an opportunity to cure.

premium channels more affordable and thus more widely available."[30] How consumers are well served by rules that would force operators to charge more for packages is not explained.

But even assuming discounts in some cases can or should be considered by the Commission, there is no indication of what the agency considers to be too steep. Discounts ranging up to 50 percent, for example, are not uncommon in the cable industry or in competing markets like sales to home satellite dish owners.[31] A safe harbor of permissible discount level is needed.

Furthermore, in order to promote the carriage of new services, substantial flexibility to create unregulated a la carte packages of these services is necessary. Consumers will be protected because new packages of new a la carte services will be affirmatively marketed. This requirement obviates the need for regulatory oversight because subscribers obviously do have a "realistic service choice" whether to take these new program offerings or not. In these circumstances, so long as each channel comprising the package can in fact be purchased individually, no governmental interest is served by imposing any restrictions on the pricing or packaging of these services.

Finally, the Commission should oust local franchising authorities from the business of deciding whether a la carte packages that meet Commission-established safe harbors are permissible. Introducing another potential layer of governmental oversight will only act to deter the introduction of services to subscribers. If questions arise regarding application of the safe harbors to a particular arrangement, the Commission should have sole jurisdiction to resolve them.

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[30] Report and Order, 8 FCC Rcd. at 5837.

[31] See Attachment B, Letter to Alexandra Wilson from Daniel Brenner, dated January 24, 1994.

III. THE COMMISSION SHOULD NOT REGULATE RATES FOR COMMERCIAL ESTABLISHMENTS

The Fifth NPRM also seeks comment on whether the Commission should "establish regulations governing rates for regulated cable service provided to commercial establishments."[32] In the Second Order on Reconsideration, the Commission concluded that it should not "establish provisions authorizing special, presumably higher, rates for regulated cable services provided to commercial establishments."[33] But in reaching this conclusion, the Commission ignored several important factors that strongly support the conclusion that rates charged to commercial establishments -- such as bars, restaurants, office buildings, and hotels -- are not subject to the same rate constraints as rates charged to residential customers. Specifically, the Commission failed to consider whether it had authority to regulate the rates charged to non-residential subscribers, whether its benchmark rates were derived from charges to those customers, and whether higher rates to commercial subscribers were warranted based on the public nature of the use of the programming supplied by the operator. When all these factors properly are taken into account, it is plain that the rates to commercial customers should not be subject to rate regulation.

A. Congress Did Not Intend to Regulate Cable System Charges to Commercial Establishments Rates

The conclusions in the Second Order on Reconsideration are based on an implicit -- and, we submit, erroneous -- assumption that Congress intended the Commission to ensure that rates for all cable customers, including commercial subscribers, should be regulated so long as the cable system does not face effective competition. However, nothing in the Cable Act or its legislative history supports the notion that Congress was concerned with cable operators' charges to commercial subscribers. As its name implies, Congress in adopting the Cable Television

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32 Fifth NPRM at ¶ 257.

33 Second Order on Reconsideration at ¶ 185.

Consumer Protection and Competition Act of 1992 focused on consumers, not businesses. There certainly is no evidence that Congress intended, in any event, that commercial subscriber rates should be identical to those charged residential households. And it makes little sense for the Commission to adopt rules that would dictate such a pricing scheme.

First, that Congress was concerned with cable service to residential, as opposed to commercial, subscribers is evident in its definition of "effective competition." The Act's tests for this purpose focus on service to "households".[34] The Commission's interpretation of a "household" makes clear that commercial customers are not included. Rather, it is based on the Census Bureau definition: "all the persons who occupy a housing unit".[35] Non-residential commercial establishments fall outside that definition.[36]

Moreover, Congress directed the Commission to adopt rules to protect "subscribers." A subscriber under the Commission's rules is "a member of the general public who receives broadcast programming by a cable television system and does not further distribute it." 47 C.F.R. Sec. 76.5(ee) (emphasis added). Commercial establishments would not be "subscribers" because they would not be a member of the general public, but instead would be a special class of businesses further distributing cable service to their patrons.[37]

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[34] See Section 623(l)(1) (emphasis added).

[35] Fourth Report and Order at ¶ 17.

[36] Under the Census Bureau definition, a "housing unit" in general is "a group of rooms or a single room that is occupied or intended for occupancy as separate living quarters; that is, the occupants do not live and eat with any other persons in the structure and there is direct access from the outside or through a common hall. Transient accommodations, barracks for workers, and institutional-type quarters are not counted as housing units." Statistical Abstract of the United States, 1993 (113th ed.).

[37] The Commission previously has found that where a "video service is delivered to hotels for resale by these establishments over internal MATV wiring to lodgers, then that service provider (i.e., the party delivering programming to the hotels [in this case, the cable operator]) has no 'subscribers' as that term is defined in the Commission's rules" because the

It makes sense that Congress did not express concern over rates charged to commercial customers in adopting the Cable Act. Commercial customers are most likely to have competitive alternatives to their local cable system through satellite dishes, MMDS, and other alternative sources. These sophisticated buyers of video service were not intended to be covered by the Act.

B. The Commission Should Not Restrict Cable Operators to Charging Commercial Customers the Same as Residential Customers

Even assuming that the Commission has jurisdiction to regulate the rates that cable operators charge their commercial customers, there is no basis for requiring operators to charge rates identical to those charged residential subscribers.

As an initial matter, the Fifth NPRM appears to assume that the rates charged to commercial subscribers are somehow reflected in the permissible rates that operators may charge residential customers.[38] This is unlikely to be the case for several reasons. Revenues from commercial establishments were not likely included by operators in completing the survey that formed the basis for the Commission's formulas.[39] The conclusion that these rates were not included is buttressed by the Commission's follow-up rate survey conducted in the aftermath of the September 1993 rate reduction, which requested data on "the charges . . . generally available to residential households."[40]

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hotel in that case would be further distributing it. Definition of a Cable Television System, 5 FCC Rcd. 7638, 7642 (1990).

[38] See Fifth NPRM at ¶ 257.

[39] That survey asked for average charges for equipment, installation and tiers charged to subscribers. FCC Cable TV Rate Survey Database, Structure of Database and Explanation Notes (rel. Feb. 24, 1993).

[40] See FCC Cable Regulation Impact Survey, Changes in Cable Television Rates Between April 5, 1993 - September 1, 1993; Report and Summary, released Feb. 22, 1994, at Appendix.

The Commission, therefore, lacks information in its benchmark rate survey from which to conclude that an operator's commercial rates are "not reasonable." There is no data on what systems subject to effective competition charge commercial establishments -- or what rate differential exists between competitive and non-competitive systems in serving commercial establishments.

As a consequence, the Fifth NPRM focuses on the wrong question in seeking comment on whether "higher earnings for commercial establishments should be offset by lower rates to other subscribers."[41] This is comparing apples and oranges. The rates that cable operators charge their residential customers are based on the rates charged to residential customers by systems subject to effective competition. Under the Commission's rate regulation theory, those rates reflect competitive conditions.

Even assuming there is some benefit to residential customers from commercial customers paying higher rates, presumably those savings are already reflected in the rates charged residential customers by competitive systems. Thus, many operators ("transitional relief" systems) have rates below the benchmark that already may reflect passed-along savings.

In any event, there are good reasons why operators should be able to charge commercial customers rates different than those charged residential subscribers. First, commercial establishments may derive a financial benefit from providing cable service to their customers. In reducing the amount that cable operators can charge them, the Commission would not reduce the ultimate rate to non-residential viewers, but merely would enable the middleman commercial customer to pocket a greater profit. There is no public interest justification for mandating such a result.

Second, in many cases, particularly where operators serve sports bars and similar businesses, programmers charge operators higher fees to reflect the benefits that these

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[41] Fifth NPRM at ¶ 257.

establishments receive from exhibiting cable programming. Therefore, an operator's costs may be higher in order to provide service to this class of customers.

For all these reasons, the Commission should not adopt rules regulating commercial rates.

CONCLUSION

For the foregoing reasons, the Commission should (1) adopt a flat fee plus programming cost methodology for adding channels to regulated tiers; (2) establish "safe harbors" for a la carte packages; and (3) leave commercial rates unregulated.

Respectfully submitted,

NATIONAL CABLE TELEVISION ASSOCIATION, INC.

By ______________________
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June 29, 1994

ATTACHMENT A

National Cable Television Association

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April 26, 1994

William E. Kennard, Esquire
General Counsel
Federal Communications Commission
1919 M Street, NW., Room 614
Washington, D.C. 20554

Re: Clarification of Federal, State and Local Jurisdiction Over Permitted Rate and Channel Changes

Dear Mr. Kennard:

On behalf of the National Cable Television Association I am writing to request clarification with respect to federal, state and local regulatory authority over changes to rates or programming on a cable operator's regulated tiers.

Section 3(f) of the 1992 Cable Act, the federal negative option billing provision, provides that "A cable operator shall not charge a subscriber for any service or equipment that the subscriber has not affirmatively requested by name." See 47 C.F.R. § 76.981. In its recent Third Order on Reconsideration the Commission held that "the Commission as well as state and local governments have concurrent jurisdiction to regulate negative option billing."[1]

We seek clarification with respect to the applicability of state or local negative option billing prohibitions to situations in which:

(1) a cable operator raises its rates (with no change in service or equipment offerings) as a result of passing through external costs or an inflation adjustment, as provided by the Commission rules;

1 Third Order on Reconsideration in MM Docket Nos. 92-966 and 92-262, FCC 94-40 (rel. Mar. 30, 1994), at ¶ 123.

(2) an operator changes its rates as a result of the addition or deletion of channels to its regulated tiers pursuant to the Commission's "going forward" regulations; or

(3) an operator replaces an existing channel of service on a regulated tier with a different channel of service, with or without a change in the rates.

We seek confirmation that, under these circumstances, the operator need not have received an "affirmative request" from its subscribers for the rate increase or channel change, i.e., that such rate increases or channel changes will not be deemed subject to the negative option billing prohibitions. Moreover, since these situations plainly "implicate 'rates for the provision of cable service'," we seek confirmation that state and local authorities are pre-empted from enacting or enforcing laws that hold such practices to be prohibited negative options.

Discussion

In the initial rate regulation Report and Order the Commission took note of the legislative history of the negative option billing provision and held that it does not apply to changes in the mix of programming on a tier.[2] Accordingly, it concluded that

> a change in the mix of channels in a tier, including additions or deletions of channels, will not be subject to the negative option billing provision unless they change the fundamental nature of the tier. We agree with CSC that operators need this flexibility to modify and upgrade their offerings in response to marketplace changes. Moreover, we do not believe that consumers necessarily expect the mix and range of services in a tier to remain static. Thus, on balance, we conclude that the consumer benefits from giving operators the ability to diversify, improve or otherwise modify their offerings in a tier outweighs the slight reduction in consumer choice that would result from exempting such changes from the negative option billing requirements.[3]

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2 Report and Order and Further Notice of Proposed Rulemaking in MM Docket No. 92-966, 8 FCC Rcd. 5631, 5906 (1993) ("Report and Order").

3 Id.